78-1242

Supreme Court, U. S.
FILED
FEB 9 1979
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM 1978

No.

INSURANCE COMPANY OF NORTH AMERICA,

Petitioner,

v.

FILOR, BULLARD & SMYTH,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

JOSEPH AUSTIN KILBOURN
Counsel for Petitioner
14 Wall Street
New York, New York 10005

Of Counsel:

BIGHAM ENGLAR JONES & HOUSTON

TABLE OF CONTENTS

	PAGE
Opinion Below	1
Jurisdiction	2
Questions Presented	2
Statute Involved	2
Statement	2
The Bond in Suit	2
The Facts	3
The Proceedings Below	4
Reason for Granting Writ	5
ARGUMENT	
I—The court below, in holding the genuine signatures unauthorized, confused the distinction between unauthorized signature and unauthorized purpose	5
II—The efficacy of all corporate signature resolutions is questioned by the lower court's decision	6
III—The Second Circuit's decision contradicts the common understanding of the term "forgery" in the business community. It is also at variance with decisional and statutory law	7
Conclusion	10
APPENDIX:	
Opinion of Court of Appeals	A1
Opinion and Order of District Court	A16
Order Denying Petition for Rehearing	A29

PAGE

Order Denying Petition for Rehearing En Banc ... A30

Order Denying Motion for Stay of Mandate A31

Judgment of Court of Appeals A32

Statute Involved A34

Example of Cashier's Check A36

TABLE OF AUTHORITIES

Cases:

Fitzgibbons Boiler Co. v. *Employers Liability Assurance Co.*, 105 F.2d 893 (C.A.2d, 1939) 9

Gilbert v. *United States*, 370 U.S. 650 (1962) 8

International Union Bank v. *National Surety Co.*, 245 N.Y. 368, 197 N.E. 269 (1927) 7, 8

People v. *Altman*, 83 Misc. 2d 771 (1975) 10

People v. *Cannarozzo*, 62 AD2d 503 (4th Dept., 1978) 9, 10

People v. *Sangiovanni*, 52 AD2d 930 (2nd Dept., 1976) 10

Regina v. *White*, 2 Car. and K. 404, 175 Eng. Rep. 167, Nisi Prius, Book 6 (1847) 8

Shapiro v. *Ferrandina*, 478 F.2d 894 (C.A.2d, 1973) 10

State Bank of Poplar Bluff v. *Maryland Casualty Co.*, 289 F.2d 544 (C.A. 8th, 1961) 9

Sunshine v. *Bankers Trust Company*, 34 NY2d 404, 314 NE 2d 860 (1974) 6

Statutes:

New York Penal Law (McKinney's, 1975) § 170.00 2, 4

New York Uniform Commercial Code (McKinney's, 1964) § 4-207(1)(b) 6

18 U.S.C. § 495 8

IN THE

Supreme Court of the United States

OCTOBER TERM 1978

No.

INSURANCE COMPANY OF NORTH AMERICA,

Petitioner,

v.

FILOR, BULLARD & SMYTH,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

TO THE HONORABLE CHIEF JUSTICE AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Petitioner, Insurance Company of North America (INA), prays that a Writ of Certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Second Circuit entered in this cause.

Opinion Below

The opinion sought to be reviewed, which has not been reported, is dated September 21, 1978 (A1).

Jurisdiction

A timely petition for rehearing *en banc* was denied on November 14, 1978 (A30) and this petition was filed within 90 days of that date. The jurisdiction of this court is invoked under 28 U.S.C. § 1254(1).

Questions Presented

1. Is the term "forgery as to a signature," as found in an insurance policy issued by INA, ambiguous?

2. Can a genuine signature, authorized by corporate resolution, be held to be "unauthorized," when made during the course of a dishonest scheme?

Statute Involved

A statute pertinent to this controversy is § 170.00 of the New York Penal Law (A34) which defines the crime of forgery.

Statement

Suit was brought by Respondent, Filor, Bullard & Smyth ("Filor"), a member firm of the New York Stock Exchange against Petitioner, INA, under a standard form No. 14 Brokers Blanket Bond. Filor claimed a loss of $963,180.50 and, in its complaint, alleged separate causes of action under dishonesty, larceny and forgery provisions of the bond. Prior to trial, three causes of action were severed and the case was tried on the forgery issue alone.

The Bond in Suit:

On or about April 17, 1969 INA issued to Filor a Form No. 14 Brokers Blanket Bond which in pertinent part provided in Insuring Clause D coverage against:

> "Loss through forgery as to a signature, or alteration of, on or in any * * * checks * * *"

The Facts:

In 1967 and 1968 Douglas J. Schotte, President of Eatontown National Bank, Eatontown, New Jersey ("Eatontown"), pursuant to a fraudulent scheme, opened brokerage accounts with Filor in the name of the bank. During the period July 3, 1967 and August, 1970 Schotte fraudulently conducted trades in these accounts in the name of the bank through the purchase and sale of numerous securities. The gross volume of these transactions was in excess of $57,000,000. During the period in question, Schotte was authorized to sign Cashier's checks of Eatontown. Section 10 of the bank's corporate bylaws provided as follows:

> "CONTRACTS
>
> SECTION 10. All contracts, checks, trusts and other instruments shall be signed by the President or a Vice President, or such other officers as may be designated by the Board of Directors."

In July and early August, 1970 Schotte placed orders with Filor to purchase various securities. Filor executed the orders and delivered (except in one instance) the securities in return for 14 Cashier's checks of Eatontown totaling $963,180.50, payable to the order of Filor and genuinely signed "Douglas J. Schotte, Auth. Sig." [See (A36) for example]

Filor endorsed the checks and deposited them in its bank for collection from Eatontown. However, on August 7, 1970, as a result of Schotte's fraud, Eatontown was declared insolvent by the Comptroller of Currency and the Federal Deposit Insurance Corporation ("FDIC") was appointed Receiver. The FDIC immediately stopped payment on the 14 Eatontown Cashier's checks totaling $963,180.50 and they were returned ultimately to Filor unpaid.

Filor thereafter filed a proof of loss with INA alleging a loss, *inter alia,* of $963,180.50 through forgery as to a signature on checks, within the purview of the Brokers Blanket Bond. INA subsequently denied liability to Filor.

The Proceedings Below:

This action was commenced on June 21, 1974 in the United States District Court for the Southern District of New York.[1] Jurisdiction was alleged by virtue of the diversity of citizenship of the two parties.

County II, III and IV of the complaint were severed prior to trial and on June 30, 1977 Count I (forgery) was tried before Judge Lawrence W. Pierce without a jury.

On August 4, 1977 Judge Pierce filed an opinion and order (A16) dismissing Count I of the complaint with prejudice and with costs. The Court held that the genuine signatures of Douglas J. Schotte were not forgeries within the meaning of § 170.00 et seq. of the New York Penal Law, nor under the case law of New York, and that the phrase "forgery" is not ambiguous.

Filor filed an appeal from the order and judgment dismissing Count I of the complaint and on September 21, 1978 the United States Court of Appeals for the Second Circuit reversed the District Court and directed that the case be remanded with instructions for the Court to enter judgment in favor of the plaintiff and against INA for $963,180.50 with interest and costs. In reversing the District Court, the Second Circuit held that the term "forgery" as used in the brokers blanket bond issued by INA to Filor, having been rendered ambiguous by recent developments in the law, must be construed against INA as the insurer. In *dicta,* the majority opined that under the present state of the law, the New York Court of Appeals would hold that Schotte's signatures were forged.

---

[1] An earlier action was brought on June 19, 1972, but was dismissed without prejudice on July 24, 1972.

INA thereafter petitioned the Second Circuit for a rehearing with a suggestion that said rehearing be held *en banc.* Orders were entered on November 14, 1978 (A29, A30) denying the petition. A motion was thereafter filed by INA in the Second Circuit seeking a stay of the mandate pending the filing of a petition for a writ of certiorari to the United States Supreme Court. This motion was denied by order dated November 29, 1978 (A31). INA then filed applications (Docket No. A-511) before Hon. Thurgood Marshall of the United States Supreme Court seeking a recall and stay of the mandate of the Second Circuit. These applications were denied on December 5, 1978.

Reason for Granting Writ

The decision of the Second Circuit is at variance with the decisional and statutory law of the State of New York and the common understanding of the business community of the term "forgery." If left standing it will create uncertainty with respect to coverage under similar insurance policies and will undermine the efficacy of all corporate signature resolutions.

ARGUMENT

I

The court below, in holding the genuine signatures unauthorized, confused the distinction between unauthorized signature and unauthorized purpose.

The Second Circuit, without any basis in fact or law, held that the genuine signatures of Douglas J. Schotte upon the Eatontown cashier's checks were "unauthorized." In order to support its holding that the term "forgery" in the brokers' blanket bond was ambiguous, it had to find the signatures unauthorized. It did so despite the fact that

Schotte was authorized to sign cashier's checks. In short, the court confused unauthorized signature with unauthorized purpose.

The New York Court of Appeals in *Sunshine* v. *Bankers Trust Company,* 34 NY 2d 404, 314 NE2d 860 (1974), recognized the distinction between unauthorized signature and unauthorized purpose. In that case the dying president of a corporation gave his wife a signed-in-blank corporate check and told her to fill it in for whatever amount she wished. She made it out for $10,000 and negotiated it. Payment was stopped and one issue in the subsequent litigation was whether the wife breached a warranty under U.C.C. § 4-207(1)(b) that she had no knowledge that her late husband's signature was unauthorized. The Court of Appeals held that she had not breached such a warranty, stating that the signature was "authorized" even though the check was not issued for an authorized purpose.

The fact that Douglas J. Schotte was not authorized to embezzle money from Eatontown has no bearing on whether he was authorized to sign checks of the bank. Obviously no one is authorized by a corporation to steal. If, during the course of an embezzlement, however, checks are drawn by an authorized signatory, the signatures are not rendered unauthorized by virtue of that person's illicit activities.

II

The efficacy of all corporate signature resolutions is questioned by the lower court's decision.

In holding, as it does, that Schotte's signatures were unauthorized, the Second Circuit has created a subjective test as to the authenticity of every corporate check. Employing the apparent test of that Court a signature is, or is not, authorized depending upon the state of mind of the drawer. If he has no fraudulent intent, the signature is

authorized. If he has a fraudulent intent, the signature is unauthorized.

Placing this decision in its proper context, even if insurers were to exclude from coverage this type of loss, a bank holding a valid signature resolution from a corporate depositor, would honor an otherwise genuine check at its peril if it turned out that the check was drawn for some illegal purpose. If the latter, the bank would have paid a check bearing an unauthorized signature and would be required to re-credit its corporate depositor's account with the amount of the check.

The impact, therefore, of the Second Circuit's decision, is not limited merely to an interpretation of forgery cover in a brokers blanket bond. It extends, by direct implication, into the relationship between all banks and their corporate depositors.

III

The Second Circuit's decision contradicts the common understanding of the term "forgery" in the business community. It is also at variance with decisional and statutory law.

The common test of "forgery" has always been whether the person making the writing puts it off as the act of another. This is the essential element of "false making." Judge Irving Lehman writing for the New York Court of Appeals in *International Union Bank* v. *National Surety Co.,* 245 N.Y. 368, 197 N.E. 269 (1927), observed at pp. 372-373:

> ". . . the courts have swept away distinctions based upon the right of a person to the use of the name, genuine or fictitious, signed by him. They have held that the test of forgery is whether a person has falsely and with purpose to defraud made a writing which purports to be the act of another. 'It would be difficult

perhaps by a single definition of the crime of forgery to include all possible cases. Forgery, speaking in general terms, is the false making or material alteration of or addition to a written instrument for the purpose of deceit and fraud. It may be the making of a false writing purporting to be that of another.' (*Commonwealth* v. *Baldwin,* 77 Mass. 197.) 'The falsity of the instrument consists in its purporting to be the note of some party other than the one actually making the signature. The falsity of the act consists in the intent that it shall pass and be received as the note of some other party.' (*Commonwealth* v. *Foster,* 114 Mass. 311.)"

The signatures of Douglas J. Schotte clearly were not forgeries under the common law. In *Regina* v. *White,* 2 Car. and K. 404, 175 Eng. Rep. 167, Nisi Prius, Book 6 (1847) the defendant, Emanuel White was charged with the offense of forgery when he endorsed a bill of exchange payable to the order of one Thomas Tomlinson "per procuration Thomas Tomlinson, Emanuel White." The Queen's Bench held that endorsing a bill of exchange under a false assumption of authority to endorse it per procuration was not a forgery, there being no false making.

The United States Supreme Court in *Gilbert* v. *United States,* 370 U.S. 650 (1962) held that an agency endorsement "Daniel Bartfield, Charline R. Bartfield, R. Milo Gilbert, Trustee" was not a forgery under 18 U.S.C. § 495 even though Gilbert had no authority from the Bartfields to endorse an income tax refund check payable to their order. Mr. Justice Harlan, speaking for the Court said at p. 657:

> "And finally, the *Regina* v. *White* view of forgery at common law was early accepted in a federal case as representing the English common law. *In re Extradition of Tully.* 20 F.812. The same view of forgery has since been followed in most of the state and federal courts in this country."

Mr. Justice, then Judge, Blackmun writing for the Eighth Circuit in *State Bank of Poplar Bluff* v. *Maryland Casualty Company,* 289 F.2d 544 (C.A. 8th, 1961) gave a clear analysis of the term "forgery" at p. 547:

> "General definitions tell us that 'forgery' means the 'act of forging, fabricating, or producing falsely,' • • •. The legal definitions place like emphasis, so far as forgery is concerned, upon 'false making or material altering' and upon something 'falsely made, imitated or forged' • • •. All this implies to us falsification and lack of genuineness in the instrument itself rather than in its content."

The Court below declined to follow its own decision in *Fitzgibbons Boiler Co.* v. *Employers Liability Assurance Co.,* 105 F.2d 893 (C.A. 2d, 1939), even though the factual setting in that case was identical to the case at bar, on the grounds that "subsequent developments in the law render the term 'forgery' ambiguous." However, the Court failed to point to any "subsequent developments" supporting this holding.

A recent case in the New York Appellate Division, Fourth Department, *People* v. *Cannarozzo,* 62 AD2d 503 (1978)[2] succinctly interpreted the revised Penal Law section defining the crime of forgery. In that case an agent of the Commissioner of Motor Vehicles wrongfully issued a chauffeur's license to the defendant who had not passed the test. The license was validated with the stamped signature of the C nmissioner of Motor Vehicles and the defendant recipient was charged with criminal possession of a forged instrument. On appeal, the court reversed the conviction stating at p. 507:

> "One does not commit the crime of forgery under section 170.00 et seq. of the Penal Law by making an

---

[2] Leave to appeal to the Court of Appeals was granted on June 28, 1978.

instrument in one's own name which falsely purports to bind another *if the maker is authorized to make the instrument,* though the recitals of the instrument be false and though the instrument be made with fraudulent intent. Since defendant's license was not a forged instrument, his conviction for possession of a forged instrument should be reversed and the indictment dismissed." [Emphasis added]

Recent cases in New York that have declined to characterize as forgeries the act of persons signing their own signatures to documents where some fraud was involved are: *People* v. *Sangiovanni,* 52 AD2d 930 (2d Dept. 1976); *People* v. *Altman,* 83 Misc. 771 (1975) and *Shapiro* v. *Ferrandina,* 478 F2d 894, 910 (CA2d, 1973).

Under the circumstances, it is clear that, contrary to the assertion of the Court below, there are no recent developments in the law that have rendered the term forgery "ambiguous." To the contrary, the term has an established and well understood meaning, both in the business world and in the law: The act of putting off one's signature, with intent to defraud, as the act of another.

Conclusion

This petition for a writ of certiorari should be granted, and the decision of the court below should be reversed.

Respectfully submitted,

JOSEPH AUSTIN KILBOURN
Counsel for Petitioner
14 Wall Street
New York, New York 10005

BIGHAM ENGLAR JONES & HOUSTON,
Of Counsel

APPENDIX

Opinion of Court of Appeals.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Nos. 567, 568—September Term, 1977.
(Argued February 27, 1978 Decided September 21, 1978.)
Docket Nos. 77-7468, 77-7488

FILOR, BULLARD & SMYTH,

Plaintiff-Appellant,

—v.—

INSURANCE COMPANY OF NORTH AMERICA,

Defendant-Appellee.

Before:

LUMBARD, FEINBERG and TIMBERS,

Circuit Judges.

Consolidated appeals, pursuant to Fed. R. Civ. P. 54(b), from an order and judgment entered in the Southern District of New York, Lawrence W. Pierce, *District Judge,* which, respectively, denied cross-motions for summary judgment and, after a bench trial, dismissed on the merits one count of a four-count complaint in a diversity action brought by the insured, a broker-dealer member of the New York Stock Exchange, to recover $963,180.50 on a brokers blanket bond, that being the loss sustained by the insured as the result of certain cashiers checks drawn and signed by the president of a bank as part of his scheme to embezzle money from the bank.

Judgment on the merits reversed; case remanded with directions to enter judgment in favor of plaintiff against defendant in amount of $963,180.50, together with interest and costs according to law.

LEWIS A. KAPLAN, New York, N.Y. (Richard Wasserman, and Paul, Weiss, Rifkind, Wharton & Garrison, New York, N.Y.), *for plaintiff-appellant.*

JOSEPH A. KILBOURN, New York, N.Y. (Bigham Englar Jones & Houston, New York, N.Y.), *for defendant-appellee.*

TIMBERS, *Circuit Judge:*

These are consolidated appeals, pursuant to Fed. R. Civ. P. 54(b), from an order and judgment entered in the Southern District of New York, Lawrence W. Pierce, *District Judge,* which, respectively, denied cross-motions for summary judgment and, after a bench trial, dismissed on the merits one count of a four-count complaint in a diversity action brought by the insured, a broker-dealer member of the New York Stock Exchange, to recover $963,180.50 on a brokers blanket bond, that being the loss sustained by the insured as the result of certain cashiers checks drawn and signed by the president of a bank as part of his scheme to embezzle money from the bank.

The question presented, which is easier to state than to resolve, is whether the checks thus drawn and signed by the president of the bank were "forgeries" as to the bank within the meaning of the brokers blanket bond issued to indemnify against loss through forgery of signatures on checks.

The district court held that the checks were not forgeries

within the meaning of the brokers blanket bond. For the reasons below, we reverse and remand.

I.

Plaintiff Filor, Bullard & Smyth ("Filor" or "the insured") is a New York partnership engaged in the business of a securities broker-dealer. It formerly was a member of the New York Stock Exchange ("NYSE").

Defendant Insurance Company of North America ("INA" or "the insurer") is a Pennsylvania corporation engaged in a nationwide insurance and surety business, including the writing of brokers and bankers blanket bonds. It wrote the brokers blanket bond here involved. It is a wholly-owned subsidiary of INA Corporation, a NYSE listed company.

Douglas A. Schotte, who drew and signed the cashiers checks here in question, was president of the Eatentown National Bank (the Bank) of Eatontown, New Jersey. Neither Schotte nor the Bank are parties to this action.

After Schotte's defalcations were discovered, the Bank was declared insolvent. The Federal Deposit Insurance Corporation (FDIC) became its receiver by operation of law. It stopped payment on the checks involved. It is not a party to the instant action. It is a party to a related action which it commenced in the District of New Jersey against Filor and others, Civ. Action No. 264-72. Proceedings on Counts Two, Three and Four of the instant action have been severed from Count One pending the outcome of the New Jersey action.

II.

The fraudulent scheme, of which the issuance of the fourteen checks here involved was a part, began in July

1967 and October 1968. During those months, Schotte, who was president and chief executive officer of the Bank, opened with Filor two brokerage accounts. They were in the name of "Eatontown National Bank, Attn: Douglas J. Schotte". Using these accounts, Schotte began trading in securities, falsely representing to Filor that he was doing so on the order, and for the account, of unidentified customers of the Bank.[1] Actually, as it later was proven, Schotte's trading in securities through the two accounts with Filor was for his own personal benefit. He used funds embezzled from the Bank to speculate in the stock market.

It is undisputed that neither Filor nor any officers, employees or directors of the Bank had any knowledge of Schotte's fraudulent scheme or of his embezzlement of Bank funds as part of the scheme.[2] It also is undisputed

---

[1] Schotte accomplished this by improperly obtaining the *full* combination to the bank vault in which the blank cashiers checks were kept. An officer in his position was entitled to only *half* the combination.

[2] The Bank's by-laws authorized its president, vice-president, and other officers designated by its board of directors to sign the Bank's contracts, checks and other instruments.

The Bank's board of directors, however, never authorized Schotte to open the accounts at Filor nor to buy and sell securities through those accounts.

The transactions underlying Schotte's defalcations, including the fourteen cashiers checks here involved, therefore, were not made on behalf of the Bank in the regular course of its business and were not carried out on behalf of the Bank's customers. Indeed, they were concealed from the Bank's other officers and directors.

Under the National Bank Act, 12 U.S.C. § 24 (Seventh) (1970), the Bank was prohibited from trading in securities for its own account. Although Schotte had general authority to sign checks on behalf of the Bank, the underlying transactions and the signing of the checks here involved were unauthorized. *Wen Kroy Realty Co.* v. *Public National Bank and Trust Co.*, 260 N.Y. 84, 89-90, 183 N.E. 73, 74 (1932).

that Schotte's acts pursuant to this scheme were dishonest, fraudulent and criminal.[3]

Schotte's defalcations were first discovered in mid-1970. The fourteen checks here involved, which aggregated $963,-180.50, were drawn and delivered by Schotte to Filor during the six day period between July 31, 1970 and August 5, 1970. Each check was drawn on the Bank and was signed by Schotte in his own name, followed by the printed legend, "Auth. Sig." The checks were delivered by Schotte to Filor in return for securities which had been ordered by Schotte pursuant to the fraudulent scheme described above.

On August 7, 1970, two days after the last of the fourteen checks referred to above was delivered by Schotte to Filor, the Bank was declared insolvent by the Comptroller of the Currency and the FDIC was appointed receiver of the Bank's assets pursuant to 12 U.S.C. § 1811, et seq. (1970).

When the fourteen checks were presented for payment by Filor to the FDIC, the latter refused payment.[4] Filor thereupon filed a proof of claim with INA on the ground that its loss was covered by the policy issued by INA because Schotte's signature was a forgery within the meaning of Clause D of the brokers blanket bond which provides that

---

[3] On August 11, 1970, Schotte was arrested and later indicted on April 20, 1971 in the United States District Court for the District of New Jersey on 168 counts of conspiracy and misapplication of bank funds. On July 25, 1972, he pleaded guilty to three counts.

[4] The FDIC refused payment on the fourteen checks on the grounds that (a) the purchases of securities for which the checks were issued were not made on the order or for the account of customers of the Bank and, in the FDIC's opinion, therefore "were illegal, void and in contravention" of statutes which prohibited such purchases; and (b) the checks were delivered in connection with a dishonest, fraudulent and criminal scheme perpetrated by Schotte and, in the FDIC's opinion, the FDIC therefore had no obligation or legal responsibility to make payment on the cashiers checks.

INA will indemnify Filor against "[l]oss through forgery as to a signature." From the district court's rejection of Filor's claim (which previously had been rejected by INA), the instant appeal has been taken. We agree with Filor and, accordingly, reverse the district court and order that judgment be entered for the full amount of Filor's claim, together with interest and costs according to law.

III.

The bond here involved is a standard form of brokers blanket bond. It not only was prepared in its entirety by INA, but each of its terms was formulated by INA and its attorneys, including the critical Clause D which covers loss through forgery of signatures on checks delivered to the insured.

Filor as a member of the NYSE was required by Rule 319 of the NYSE to obtain and have in effect such a bond to insure against loss through check forgeries, inter alia, as a condition of doing business as a broker-dealer.[5]

---

[5] The history of the present Rule 319 of the NYSE goes back nearly forty years to the defalcations of Richard Whitney as president of the NYSE. See Report of the Securities and Exchange Commission, pursuant to Section 21(A) of the Securities Exchange Act, dated November 1, 1938, in the *Matter of Richard Whitney, et al.*

While much time was spent in the district court regarding Filor's offer of, and INA's objections to, evidence of the history and purpose of the bond requirement reflected in the present Rule 319, we take judicial notice that one of the business purposes of Rule 319 is to require member firms dealing with the public to carry insurance coverage against losses through check forgery. See Report of NYSE Public Examining Board on Consumer Protection, under heading "Specific Recommendations for Greater Customer Protection" at 10, 16-17 (1939). The Board that made this Report was appointed in 1939 by William McChesney Martin, then president of the NYSE.

Insuring Clause D of the brokers blanket bond here involved provided in relevant part that INA would indemnify Filor against:

> "Loss through forgery as to a signature, ... on or in any . . . checks . . . which are directed to the Insured and authorize . . . the transfer, payment, delivery or receipt of any funds or Property and bear the forged signature of . . . any customer, stockbroker, banker or other financial institution. . . ."

The issue thus presented is whether Schotte's action in drawing and signing the fourteen cashiers checks constituted forgery as to the signature of the Bank within the meaning of Clause D of the brokers blanket bond.[6]

Filor contends that Schotte "forged" the checks within the present meaning of New York law; and that INA therefore must indemnify it for losses sustained, inasmuch as INA's blanket brokers bond protects Filor against "loss through forgery." Alternatively, Filor contends that "forgery" as used in the blanket brokers bond is ambiguous in view of recent developments in the law; and that it therefore must be construed against INA as the insurer.

---

[6] At the time of Schotte's defalcations here involved, there were in effect two other bonds issued by INA to the Bank, i.e. other than the brokers blanket bond which is the subject of this case: an employee dishonesty blanket bond and a bankers blanket bond. Both insured the Bank in substance against loss through "dishonest, fraudulent or criminal act[s]" of its employees. After Schotte's scheme was discovered and the Bank was placed in receivership, the receiver, FDIC, made a claim on the INA bonds for losses allegedly sustained by the Bank by virtue of Schotte's activities. In connection with that claim, INA entered into an agreement which specifically acknowledged that the fourteen cashiers checks here at issue constituted "potential . . . losses *covered by said bonds*" and, therefore, that the issuance of those checks by Schotte constituted "dishonest, fraudulent or criminal act[s]" (emphasis added). As the district court concluded, "There is no dispute that Schotte's acts were dishonest, fraudulent and criminal."

In reversing the district court and remanding with directions to enter judgment for Filor, we rest our decision on Filor's alternative contention. As explained below, however, we shall indicate our views on that issue, albeit by way of dictum.

IV.

Turning to what we regard as the decisive issue in the case, we take it to be common ground that an ambiguous term in an insurance contract must be construed against the insurer which wrote the contract. Since New York substantive law is controlling, we note that the New York Court of Appeals follows the generally accepted rule stated above:

> "[*T*]*he burden* in such a case as this *is on the defendant to establish that the words and expressions used* [*in the policy*] *not only are susceptible of the construction sought by defendant but that it is the only construction which may fairly be placed on them.* The defendant in its large illuminated lettering and in its application could have added proper, unambiguous words or a definition . . . thus removing the ambiguity or equivocal character of the invitation to insure, of the application for insurance and the contract of insurance itself." *Lachs* v. *Fidelity & Casualty Co. of New York,* 306 N.Y. 357, 365-66, 118 N.E.2d 555, 559 (1954) (emphasis added).

We have applied this rule where appropriate. *See, e.g., Pan American World Airways, Inc.* v. *Aetna Casualty & Surety Co.,* 505 F.2d 989, 999-1000 (2 Cir. 1974).

The narrow issue for determination, therefore, is whether INA's construction of "forgery" is the only fair one that could be placed on that term at the time the blanket bond was written. Although an unauthorized signature may not

have constituted a forgery under New York law at the time of our decision in *Fitzgibbons Boiler Co.* v. *Employers' Liability Assurance Co.,* 105 F.2d 893 (2 Cir. 1939), discussed more fully *infra,* subsequent developments in the law, also discussed more fully *infra,* render the term "forgery" ambiguous as applied here.

Prior case law regarding losses which result from an unauthorized signature indicates that the circumstances surrounding Filor's loss were neither unique nor unforeseeable. Moreover, the nature of this risk is such that it could have been identified and described with particularity. INA was aware of the ambiguity of the term "forgery". It was in the best position to eliminate the ambiguity. The blanket brokers bond was in the standard form, drafted by INA, which had notice that the term "forgery" was ambiguous. INA's attorneys were aware of the conflicting decisional law, discussed more fully *infra,* reflecting the ambiguity of the term "forgery". *See, e.g.,* Maurice, *Recent Developments in Claims under Blanket Bonds,* 1965 Proc. ABA Ins. Section, at 27; Maurice, *Forgery in the Law of Insurance,* 1960 Proc. ABA Ins. Section, at 81; Farnsworth, *Insurance Against Check Forgery,* 60 Colum. L.Rev. 284, 313-16 (1960). Nevertheless, in drafting Insuring Clause D, INA failed to refer to or to exclude a loss resulting from an unauthorized signature.

Our construction of the term "forgery" in favor of the insured also strikes us as being in accord with the intent of the parties. Absent a specific exclusion, Filor reasonably could have assumed that the blanket brokers bond covered a known risk such as a loss sustained as the result of an unauthorized signature. Indeed, INA fails to suggest any other type of "forgery" to which this coverage of the bond applies. And, as indicated above, Filor was required by Rule 319 of the NYSE to obtain and maintain in effect this bond to insure against loss through check forgeries. This

rule obviously is intended to protect member firms and the public investor against precisely the type of loss here involved. The rule specifically so provides.

We hold that the term "forgery" as used in the blanket brokers bond, having been rendered ambiguous by recent developments in the law, must be construed against INA as the insurer, and that judgment accordingly must be entered in favor of Filor.

V.

This brings us to the other ground, referred to above, upon which appellant relies for reversal, namely, that the New York courts would hold that the fourteen cashiers checks here involved were "forged" as a matter of law.

Having ruled that judgment must be entered in favor of appellant on the alternative ground that recent developments in the law have rendered ambiguous the term "forgery" as used in this bond, our discussion under this section of our opinion is dictum. We believe it is appropriate for us to state our views on this issue, however, because it does have some bearing on the alternative ground upon which we have ruled in favor of appellant.

The district court, in deciding the case in favor of appellee, quite understandably relied heavily on our decision in *Fitzgibbons Boiler Co.* v. *Employers' Liability Assurance Co.*, 105 F.2d 893 (2 Cir. 1939) (A.N. Hand, J.). There we held that unauthorized action by a corporate officer in signing corporate checks did not constitute forgery, so long as the officer's signature was genuine as it appeared on the checks. In so holding, we were merely attempting fairly to state New York law as it then existed. New York law, however, has changed. And although *Fitzgibbons* probably stated New York law accurately in 1939, there are substantial reasons for doubting its viability today.

First, in 1967 New York substantially revised its penal law concerning forgery to including writings unauthentic because not authorized.[7] The only New York state court decision, so far as we know, which has addressed the question of an unauthorized signature on behalf of a corporation under the amended statute is *People* v. *Dairylea Cooperative, Inc.* (unreported) (Sup. Ct., Albany Co., 1975), *aff'd*, 52 A.D.2d 1004, 383 N.Y.S.2d 877 (3d Dept. 1976), where the Supreme Court in dictum stated:

> "The essential element of forgery has to do with the making of the instrument . . . . The defendant must have falsely made the document *(pretending to have authority of a real nature when he does not);* 'falsely completed' the document . . .; or 'falsely altered' the document . . ." (slip op. at 14-15, October 16, 1975) (emphasis added).

Second, the Model Penal Code makes explicit the drafters' intention to overrule *Fitzgibbons*. See American Law Institute, Model Penal Code, Commentary to § 223.1 [later § 224.1], 83 n. 18 (Tent. Draft No. 11, 1960).[8]

---

[7] As amended in 1967, the New York Penal Law in relevant part provides:

> "A person is guilty of forgery in the third degree when, with intent to defraud, deceive or injure another, he *falsely makes*, completes or alters a written instrument." N.Y. Penal Law § 170.05 (McKinney 1975) (emphasis added).
>
> * * * * *
>
> "A person 'falsely makes' a written instrument when he makes or draws a complete written instrument in its entirety, or an incomplete written instrument, which purports to be an authentic creation of its ostensible maker or drawer, but which is not such either because the ostensible maker or drawer is fictitious or *because, if real, he did not authorize the making or drawing thereof.*" N.Y. Penal Law § 170.00, Subd. 4 (McKinney 1975) (emphasis added).

[8] Section 224.1 of the Model Penal Code, which is substantially

(footnote continued on following page)

Third, courts in California, Michigan, and Illinois[9] appear to favor including actions such as Schotte's within the scope of forgery.

For these reasons, if we were required to decide this case on this ground, we would hold that *Fitzgibbons* no longer reflects New York law as it now exists and that the New York Court of Appeals probably would hold that the fourteen cashiers checks were "forged" as a matter of law. In view of the alternative ground upon which we have rested our decision, however, we follow the preferred practice of our Court[10] of not anticipating rulings of the New York courts when we are not required to do so.[11]

(footnote continued from preceding page)

the same as the New York Penal Law, note 7 *supra*, provides that a person is guilty of forgery if he

> "makes, completes, executes, authenticates, issues or transfers any writing so that it purports to be the act of another *who did not authorize that act. . . .*" Model Penal Code § 224.1 (Prop. Off'l Draft 1962) (emphasis added).

The Commentary to this section states:

> "An important doctrine of forgery law by which the offense is distinguished from ordinary false pretense is the requirement that the falsity relate to authenticity. . . . [W]here an instrument purports to be executed by an agent, the prevailing rule, *which we propose to change*, is that there is no forgery even if the agent knew he lacked an authority." Model Penal Code § 223.1 [later § 224.1], comment (Tent. Draft No. 11, 1960) (emphasis added).

[9] *Century Bank* v. *St. Paul Fire and Marine Ins. Co.*, 4 Cal. 3d 319, 482 P. 2d 193 (1971); *People* v. *Sousalla*, 392 Mich. 387, 220 N.W. 2d 405 (1974); *People* v. *Young*, 19 Ill. App. 3d 455, 311 N.E. 2d 609 (1974).

[10] *Wilson* v. *Fogg*, 571 F.2d 91, 95 (1978); *Cameron* v. *Fastoff*, 543 F.2d 971, 978 & n. 7 (1976).

[11] In view of our rulings above, we find it unnecessary to reach appellant's claims of error based on the district court's exclusion of evidence asserted to be relevant to construing the blanket brokers bond here involved.

Reversed and remanded with directions to enter judgment in favor of plaintiff against defendant in amount of $963,180.50, together with interest and costs according to law.

LUMBARD, *Circuit Judge* (concurring):

Decision in this appeal turns upon whether unauthorized but otherwise genuine signatures are "forgeries" under New York law. In this diversity action, the brokerage firm of Filor, Bullard & Smyth [Filor] seeks to recover from its insurer, Insurance Company of North America [INA], losses Filor suffered when Douglas Schotte, formerly President of Eatontown National Bank, wrote fourteen unauthorized cashier's checks to the order of Filor. Using the funds so obtained, Schotte began trading in securities for his own personal benefit, falsely representing to Filor that he was trading on behalf of unidentified customers of the bank. The parties agree that New York law governs this case. Appellant Filor claims that Schotte "forged" the checks within the present meaning of New York law, and that INA must therefore recompense Filor for the losses incurred, inasmuch as Filor's contract with INA protects against "loss through forgery." Alternatively, Filor seeks to show that the meaning of the word "forgery" as used in its insurance bond is ambiguous and must therefore be construed against the insurer. Since we all agree that recent developments in New York law have rendered the scope of the term "forgery" ambiguous with respect to Schotte's defalcations, and that appellant Filor is therefore entitled to recover on its insurance bond, we need not anticipate the New York courts on an unsettled question of New York law.

To be sure, at one time New York law seemed relatively clear on this point. In *Fitzgibbons Boiler Co.* v. *Employers'*

Liability Assurance Co., 105 F.2d 893 (2d Cir. 1939), this court held that unauthorized action by a corporate officer in signing a corporate check was not forgery, so long as the officer's signature was genuine. In so holding, this court attempted to state New York law as it then existed. But New York law on this point has since changed.

In 1967 New York revised its statutory definition of forgery to include writings inauthentic because not authorized. New York Penal Law § 170.00[4]. In framing this revision, the New York legislature followed the approach adopted by the Model Penal Code. *Compare* ALI, Model Penal Code § 224.1 (Proposed Official Draft 1962). The commentary to the Model Penal Code makes explicit the drafters' determination to overrule *Fitzgibbons*. ALI, Model Penal Code, Commentary to § 223.1, 83 n.18 (Tent. Draft No. 11, 1960). Thus *Fitzgibbons* is no longer consistent with New York statutory law.

New York case law has also departed from the view articulated in *Fitzgibbons*. Although New York case law is by no means conclusive on the question whether unauthorized but otherwise genuine signatures are forgeries, dictum in *People* v. *Dairylea* (Sup. Ct. Albany Co., 1975), *aff'd*, 52 App. Div. 2d 1004, 383 N.Y.S.2d 877 (3d Dept. 1976), follows the Model Penal Code view. Courts in California, Michigan, and Illinois, furthermore, favor including malefactions such as Schotte's within the scope of forgery. *See, e.g., People* v. *Young*, 19 Ill. App. 3d 455, 311 N.E. 2d 609 (1974).

That these developments in statutory and case law have rendered the term "forgery" ambiguous as used in Filor's insurance bond is by itself sufficient to require reversal of the court below and judgment for appellant Filor. As with the drafter of any contract, the insurer pays the price of ambiguity. *See Pan American World Airways, Inc.* v. *Aetna Casualty & Surety Co.*, 505 F.2d 989, 999-

1000 (2d Cir. 1974); *Lachs* v. *Fidelity & Casualty Co. of New York*, 306 N.Y. 357, 365-66, 118 N.E. 2d 555, 559 (1954). Under New York law, the term "forgery" is at least ambiguous enough to encompass genuine but unauthorized signatures. INA, moreover, was undoubtedly aware of the ambiguity in its agreement with Filor, *see, e.g.*, Maurice, Recent Developments in Claims Under Blanket Bonds, *1965 Proc. ABA-Ins. Section*, at 27, and could easily have avoided any uncertainty by inserting clarifying language in the bond which it drafted.

Having found the meaning of the term "forgery" ambiguous under New York law, we need not—and should not—hazard a prediction of what the New York courts will do when and if they reach this issue. When a case may be decided on other grounds, federal-state comity requires that federal courts refrain from unnecessarily anticipating state court decisions.

Opinion and Order of District Court.

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

74 Civ. 2597
46256

FILOR, BULLARD & SMYTH,

Plaintiff,

v.

INSURANCE COMPANY OF NORTH AMERICA,

Defendant.

APPEARANCES:

LEWIS A. KAPLAN, Esq.
RICHARD WASSERMAN, Esq.
PAUL, WEISS, RIFKIND, WHARTON
& GARRISON
345 Park Avenue
New York, New York 10022

Attorneys for Plaintiff

JOSEPH A. KILBOURN, Esq.
BIGHAM ENGLAR JONES & HOUSTON
14 Wall Street
New York, New York 10005

Attorneys for Defendant

LAWRENCE W. PIERCE, D.J.

Opinion and Order of District Court.

OPINION AND ORDER

This diversity action brought upon a Brokers' Blanket Bond presents the question of whether the actual signature of an employee affixed to a check in the course of embezzlement from the employer constitutes a forgery under New York law. The matter having been tried without a jury and the Court having considered the applicable law, the Court now concludes that no forgery is presented and that judgment should be entered for the defendant on Count One of the complaint. The following are findings of fact and conclusions of law set forth pursuant to Rule 52(a) Fed.R.Civ.P.

Findings of Fact

The facts necessary to the Court's decision herein are undisputed. This action was commenced by plaintiff Filor Bullard & Smyth ("Filor"), a partnership existing under the laws of New York State, against its carrier, defendant Insurance Company of North America ("INA"), to recover $963,180.50 plaintiff claims to have suffered as the result of the federally-declared insolvency of the Eatontown National Bank, Eatontown, New Jersey. Plaintiff claims that fourteen cashier's checks issued and signed by Douglas A. Schotte, then president of the Eatontown Bank, in the course of Schottt's defalcations, were "forged" within the meaning of Clause D of the Brokers' Blanket Bond issued to plaintiff by defendant.

Plaintiff's complaint contains four claims for relief. However, by consent order dated February 8, 1977, Counts Two through Four were severed from Count One and stayed until the outcome of related litigation brought by the Federal Deposit Insurance Corporation ("FDIC") against Filor and others in the United States District Court for the District of New Jersey (Civ. Action No.

264-72). Thus the sole issue at trial here was whether Schotte's acts were forgeries within the meaning of the Bond.

Douglas Schotte was chief executive officer of the Eatontown Bank and was responsible for the bank's daily operations and management. Section 10 of the Eatontown By-Laws granted Schotte unlimited authority to sign checks of the bank.

> "All contracts, checks, drafts and other instruments shall be signed by the President or a Vice President, or such other officer as may be designated, by the Board of Directors." (DX-M)

In July 1967 and October 1968, Schotte opened with Filor two brokerage accounts in the name "Eatontown National Bank, Attn: Douglas J. Schotte." (DX-A and DX-B). During the time at issue, the Eatontown Bank was empowered by the Comptroller of the Currency with trust powers permitting it to trade in securities upon the orders of its customers. However, Eatontown in fact had no trust department. Nevertheless, it is undisputed that at all times Filor dealt with Schotte under the mistaken impression that Eatontown was trading securities on the order and for the account of unidentified customers of Eatontown. Such activity would have been permissible under the National Bank Act, which provides in pertinent part as follows:

> "Seventh . . . The business of dealing in securities and stock by the association shall be limited to purchasing and selling such securities and stock without recourse, solely upon the order, and for the account of, customers, and in no case for its own account . . . ." (12 U.S.C. § 24).

In fact, the stock purchases made by Schotte were not upon the order or for the account of any bank customer and the Eatontown Board of Directors never granted Schotte authority to make such purchases. Rather, the Schotte transactions ultimately proved to have been part of an illegal scheme by Schotte to embezzle funds of the bank to cover his own trading losses and to speculate in securities for his own benefit. There is no dispute that Schotte's acts were dishonest, fraudulent and criminal.

The fourteen cashiers checks at issue here (PX-2 through PX-15) were each drawn on the Eatontown Bank and signed by Schotte in his own name. Each signature was followed by the printed legend "authorized signature". The checks were signed and transmitted to Filor between July 31, 1970 and August 5, 1970. On August 7, 1970, the Comptroller of the Currency declared the Eatontown Bank insolvent and the FDIC was appointed receiver of the assets pursuant to 12 U.S.C. § 1811, et seq.

When Filor presented the cashiers checks to the FDIC for payment, the latter refused to recognize the checks as valid obligations of Eatontown. Filor then filed a proof of claim with defendant INA, asserting that the signature of Douglas Schotte was a "forgery" within the meaning of the Brokers' Blanket Bond. Filor also claimed that the loss was covered by other provisions of the policy covering dishonest acts of employees and larceny. Clause D of the Bond provides that the policy covers:

> "Loss through forgery as to a signature or alteration of, on or in any bills of exchange, checks, drafts, acceptances, certificates of deposit or other written orders or directions to pay sums certain in money, due bills, money orders, warrants, orders upon public treasuries, letters of credit, written instructions or advices which are directed to the Insured and authorize or acknowledge the transfer, payment, delivery or re-

ceipt of any funds or Property and bear the forged signature of, or have been altered without the consent of any customer, stockbroker, banker or other financial institution, withdrawal orders or receipts for the withdrawal of funds or property, or receipts or certificates of deposit for Property and bearing the name of the Insured as issuer, excluding, however, coupon and serial notes, bonds, script, debentures and obligation of a similar nature and whether registered or unregistered, and coupons attached thereto or detached therefrom.

"Any check or draft (a) made payable to a fictitious payee and endorsed in the name of such fictitious payee or (b) procured in a face to face transaction with the maker or drawer thereof or with one acting as agent of such maker with the maker or drawer thereof or with one acting as agent of such maker or drawer by anyone impersonating another and made or drawn payable to the one so impersonated and endorsed by any one other than the one impersonated, shall be deemed to be forged as to such endorsement.

"Mechanically reproduced facsimile signatures are treated the same as handwritten signatures." (PX-25)

On August 11, 1970, Douglas Schotte was arrested and formally charged with misapplication of bank funds. He subsequently pleaded guilty to three counts of a 168-count indictment filed in the U.S. District Court for the District of New Jersey. Schotte was not charged with forgery.

The above facts are the only findings necessary to the Court's decision. The parties offered other evidence on the details of the relationship between Filor and Eatontown, on the question of Filor's diligence or lack thereof in dealing with and investigating Schotte, and on assorted different insurance policies addressing coverage as to for-

gery. Plaintiff Filor also presented evidence showing that it was required to purchase a Brokers' Blanket Bond by New York Stock Exchange Rule 319, and illustrating that the Bond was drafted by INA and not subject to negotiation as to its terms. Finally, Filor offered some evidence in an attempt to demonstrate that INA was aware of the issue of whether or not an agent's unauthorized signature constitutes a forgery under New York law. The Court ruled much of this evidence irrelevant at trial and now concludes that all of these subsidiary questions are unimportant to the single legal question presented in this case, to wit, whether or not Schotte's acts constituted forgery.

Conclusions of Law

The parties are citizens of different states and the amount in controversy satisfies the statutory requirement of 28 U.S.C. § 1332. Thus, the Court has subject matter jurisdiction.

Plaintiff Filor argues that the signatures of Schotte were forgeries since he was representing to Filor that he had authority to issue the checks when in fact he did not. In the alternative, plaintiff argues that the term "forgery" in Clause D of the Bond is ambiguous and that it should be construed against the drafter of the policy, INA. Defendant urges that Schotte's acts were authorized by the Eatontown by-laws and that even if they were not, no forgery is presented. INA also argues that the term "forgery" must be given its plain meaning under the law and that it is thus not ambiguous.

Both parties agree, and it is clear to the Court, that the term "forgery" in the Bond must be explicated by reference to the New York Penal Law in effect in 1969 when the Bond was issued. N.Y. Penal Law Section 170.00(4) (McKinney 1975) provides as follows:

"A person 'falsely makes' a written instrument when

> he makes or draws a complete written instrument in its entirety, or an incomplete written instrument, which purports to be an authentic creation of its ostensible maker or drawer, but which is not such either because the ostensible maker or drawer is fictitious or because, if real, he did not authorize the making or drawing thereof."

The Practice Commentaries to this section, drawn from the legislative history of the 1967 revision of the statute, purport to set forth five samples illustrating "every true form of forgery." The situation presented here is conspicuous by its absence. Thus reference must be made to the case law.

In *Regina* v. *White,* 2 Car. & K. 404, 175 Eng.Rep. 167 (Nisi Prius, Book 6) (1847), defendant White was convicted of forgery when he endorsed a check payable to the order of one Thomas Tomilson as follows: Per procuration Thomas Tomilson, Emanuel White." White signed his own name, but he in fact had no agency authority to act for Tomilson. The conviction was reversed on appeal, the court holding as follows:

> "[I]ndorsing a bill of exchange under a false assumption of authority to indorse it per procuration is not forgery, there being no false making." (2 Car. & K. at 412, 175 Eng.Rep. at 170).

Lord Chief Justice Wilde explained the principle by the following simple illustration:

> "If a man write in his own name, 'I have authority to obtain such and such goods from you'; that would not be a forgery even if he had no such authority." (*Id.* at 408, 175 Eng.Rep. at 169)

Plaintiff argues that *Regina* v. *White* is no longer valid authority since the rule laid down in that case was changed by statute in the United Kingdom years ago. See *Gilbert* v. *United States,* 370 U.S. 650, 655-56 (1961). In any event, the result herein is controlled not by English law but by the law of the State of New York. As the discussion will indicate, the New York law of forgery has deep roots in the common law, including the decision in *Regina* v. *White.*

In 1961 the United States Supreme Court was faced with the same issue in construing the federal forgery statute, 18 U.S.C. § 495. Justice Harlan, writing for the Court in an opinion joined by only three other Justices, held that the purported agency endorsement "Daniel H. Bartfield, Charline R. Bartfield, R. Milo Gilbert, Trustee" did not constitute a forgery where Gilbert signed his own name, even though he was exceeding his authority over the Bartfields' checks. *Gilbert* v. *United States,* 370 U.S. 650 (1961). Relying upon *Regina* v. *White* and several common law decisions in different states, the Court held that

> "where the 'falsity lies in the representation of facts, not the genuineness of execution' it is not forgery." (*Id.* at 658, quoting *Marteney* v. *United States,* 216 F.2d 760, 763-64 (10th Cir. 1954))

As plaintiff notes, the *Gilbert* decision construed federal law, not the New York Penal Law and thus plaintiff asserts that it is necessary to examine the case law of the state.

As plaintiff Filor points out, the New York Penal Law was revised in 1967, yet it is to be noted that plaintiff relies almost exclusively upon New York decisions rendered long before the revision of the statute, such as *Schramm* v. *Metropolitan Casualty,* 224 App. Div. 573, 231 N.Y.S. 554 (1st Dept. 1928). There the president of a company endorsed checks made by the plaintiff to the order of the

president's employer. The president had no authority to endorse checks; that power was granted to the firm's treasurer only. The president further embezzled the proceeds. Plaintiff Schramm brought suit against its insurance carrier to recover on a policy insuring plaintiff against losses due to forgery. The case was submitted to the Appellate Division on undisputed facts. The court directed that judgment should be entered for the plaintiff, however, in doing so the decision relied upon an "important part of the submitted facts" which read as follows:

> "That a loss resulting from the act of a corporate officer in endorsing a check without authority and appropriating the proceeds shall be deemed a loss within the meaning of said bond, whether or not such unauthorized endorsement technically constituted forgery within the meaning of the Penal Law . . . ." (231 N.Y.S. at 556)

Upon this set of facts, the court concluded that the loss was covered by the policy. The decision also concluded that the acts of the embezzler constituted forgery since he was unauthorized to endorse checks. However, since the latter conclusion was not necessary to the decision, that portion of the *Schramm* opinion must be regarded as mere dictum.

Even if the *Schramm* decision can be read to stand for the conclusion that the president's unauthorized signature was a forgery under New York law, that interpretation does not support the plaintiff's position here. While it appears that neither Schotte nor the embezzler in *Schramm* had legal authority to engage in defalcations for their respective principals, see *Wen Kroy Realty Co.* v. *Public National Bank,* 260 N.Y. 84 (1932); Restatement of Agency (2d) § 235, Schotte, unlike the embezzler in *Schramm,* did have corporate authority to sign checks. Accordingly the *Schramm* decision is inapposite, even assuming that the court's *obiter* represents the law of the State of New York.

This is not to suggest that the law on the issue is clear. Decisions cited by the plaintiff do indicate that some courts might conclude that Schotte's acts were forgeries. See *International Union Bank* v. *National Surety Co.,* 245 N.Y. 368, 373 (1927); *Wagner Trading Co.* v. *Battery Park National Bank,* 228 N.Y. 37, 42-43 (1920); *Century Bank* v. *St. Paul Fire & Marine Insurance Co.,* 93 Cal.Rptr. 569, 482 F.2d 193 (1971). However, this Court considers itself bound by the Circuit Court's construction of New York law, *Fitzgibbons Boiler Co.* v. *Employers' Liability Assurance Corp.,* 105 F.2d 893 (2d Cir. 1939,.

In *Fitzgibbons,* Judge Augustus Hand reviewed the common law and the law of New York in determining an issue remarkably similar to that presented here. In that case, one Anthony T. Miano, an assistant treasurer of the plaintiff, signed checks in his own name and then presented the instruments to two other officers of the company for their counter-signatures. All of the signatures were genuine; however, Miano signed his own name and procured the other signatures in the course of a scheme to embezzle the funds. Judge Hand, for the court, affirmed the dismissal of plaintiff's insurance claim against its carrier, rejecting the view that Miano's acts constituted "forgery" within the meaning of the bond and under New York law. The court concluded as follows:

> "[A] instrument purporting to be executed by one as agent of a principal therein named was not forged, though the agent in fact had no authority to execute it." (105 F.2d at 896)

Like Douglas Schotte in this case, Anthony Miano in *Fitzgibbons* had general authority to execute contracts on behalf of the corporation. 105 F.2d at 895. The Court is

not persuaded by plaintiff's attempts to distinguish *Fitzgibbons* from the facts presented here.

Plaintiff Filor offers scant support for its interpretation of the language of the 1967 Penal Law that an unauthorized but genuine signature constitutes a forgery. Filor concedes that there is no New York decision since 1967 which addresses the exact issue presented here, and the only case Filor can cite contains but dicta, since in that decision the court dismissed the forgery counts on other grounds. See *People* v. *Dairylea Cooperative, Inc.* (unreported) (Sup.Ct. Albany Co. 1975), *aff'd mem.* 52 App. Div.2d 1004, 383 N.Y.S.2d 877 (3d Dept. 1976).

Plaintiff argues that since Schotte was engaged in embezzlement from his employer and because the National Bank Act barred the Eatontown Bank from trading in securities for its own account, Schotte's signature was a forgery of his corporate office. Filor posits that the phrase "the maker or drawer . . . did not authorize the making thereof" (N.Y. Penal Law § 170.00(4)) thus compels the conclusion that Schotte's illegal acts were forgeries. In this Court's view, Filor's argument would expand the scope of the Penal Law to include every embezzlement where the defalcator signed his own name in the course of stealing from his employer. The cases cited by the plaintiff at best lead to the conclusion that the final phrase of N.Y. Penal Law § 170.00(4) describes a situation where the employee exceeds his corporate authority, i.e., where he signs a check in the absence of a corporate resolution granting him the power to sign such instruments. Here Schotte had such corporate authority. The fact that Schotte had no legal authority to commit the embezzlement does not mean that his signatures were "not authorize[d]" in the sense that the Penal Law employs that term.

The Court finds no direct support for plaintiff's claim that the 1967 revision of the Penal Law in effect overrules

the principle passed down from *Regina* v. *White*, through *Gilbert* v. *United States* to *Fitzgibbons*. Indeed, *Fitzgibbons* recently has been applied to a case arising after the 1967 revision of the forgery statute. *Rondout National Bank* v. *The Aetna Casualty & Surety Co.*, 72 Civ. 2934 (S.D.N.Y. Nov. 28, 1975). In *Rondout*, the insured claimed that stock pledged to it as collateral had been stolen from the issuer and posted without authority. Thus, argued the insured bank, it sustained a loss due to forgery when the stock turned out to be worthless. Judge Griesa dismissed the claim after trial, concluding that the signatures on the stock were genuine and affixed by corporate officers of the issuer prior to the alleged theft. The court stated as follows:

> "I also find that there was no forgery within the meaning of the bond . . . . [I]t is the law in this state that there is no forgery of a signature where the genuine signature of the person whose signature is questioned appears on the instrument. The citation for the point is *Fitzgibbons Boiler Co.* v. *Employers' Liability Assurance Corp.*, 105 F.2d 893, Second Circuit case decided in 1939." (*Id.*, Tr. at 14)

The Court concludes that the facts presented here do not constitute a "forgery" within the meaning of the Brokers' Blanket Bond.

The Court rejects plaintiff's alternative argument that the phrase "forgery" is ambiguous and that it thus should be construed against INA. Terms in insurance contracts are to be given their plain and ordinary meaning. *Kramer Grocery Co.* v. *Glen Falls Insurance Co.*, 497 F.2d 709, 711 (8th Cir. 1974); *Bristol Steamship Corp.* v. *London Assurance*, 404 F.Supp. 749 (S.D.N.Y. 1975). The fact that reference must be made to the common law and to the law of New York in order to ascertain the meaning of the word

Opinion and Order of District Court.

"forgery" does not mean that the term is ambiguous. See *Mustang Beach Development Corp.* v. *Fidelity & Casualty Co. of New York,* 348 F.Supp. 1270 (S.D. Tex.), *aff'd,* 463 F.2d 1135 (5th Cir. 1972). The phrase "forgery" is not ambiguous, and so much of the Court's order dated February 19, 1976, which stated to the contrary in denying the cross-motions for summary judgment, is overruled.

Filor's final argument, that public policy and the protection of investors mandates a broad reading of the Bond, is rejected as an unwarranted invitation to expand the scope of the policy through judicial construction. See *Zipperer* v. *State Farm Mutual Automobile Insurance Co.,* 254 F.2d 853, 856 (5th Cir. 1958). As defendant suggests, a judgment for INA on Count One does not mean that Filor will be totally uncompensated for its losses. Clause A of the Bond, covering dishonesty losses, might well reach the acts at issue here, and result in at least partial compensation to plaintiff. However, plaintiff's claim based on Clause A is contained in Count Two of the complaint, which is not before the Court at this time.

For the foregoing reasons, judgment should be entered for the defendant dismissing Count One with prejudice and with costs. There being no just reason for delay, Rule 54(b) Fed.R.Civ.P., counsel for the defendant is directed to submit an appropriate order of judgment on five days' notice.

So Ordered.

Dated: New York, New York
August 4, 1977

Lawrence W. Pierce
U. S. D. J.

Order Denying Petition for Rehearing.

UNITED STATES COURT OF APPEALS

Second Circuit

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Court House, in the City of New York, on the fourteenth day of November, one thousand nine hundred and seventy-eight.

Present: Hon. J. Edward Lumbard
Hon. Wilfred Feinberg
Hon. Williams H. Timbers

Circuit Judges.

77-7468

Filor, Bullard & Smith

Plaintiff-Appellant

v.

Insurance Company of North America

Defendant-Appellee

A petition for a rehearing having been filed herein by counsel for the defendant-appellee

Upon consideration thereof, it is

Ordered that said petition be and hereby is Denied.

A. Daniel Fusaro
A. Daniel Fusaro
Clerk

Order Denying Petition for Rehearing En Banc.

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

At a stated term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Court House, in the City of New York, on the fourteenth day of November, one thousand nine hundred and seventy-eight.

FILOR, BULLARD & SMYTH

Plaintiff-Appellant

v.

INSURANCE COMPANY OF NORTH AMERICA

Defendant-Appellee

A petition for rehearing containing a suggestion that the action be reheard en banc having been filed herein by counsel for the defendant-appellee, and no active judge or judge who was a member of the panel having requested that a vote be taken on said suggestion,

Upon consideration thereof, it is

Ordered that said petition be and it hereby is DENIED.

Irving R. Kaufman

IRVING R. KAUFMAN, Chief Judge

Order Denying Motion for Stay of Mandate.

77-7468
#719

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Court House, in the City of New York, on the 27th day of November, one thousand nine hundred and seventy-eight.

FILOR, BULLARD & SMYTH,

Plaintiff-Appellant,

v.

INSURANCE COMPANY OF NORTH AMERICA,

Defendant-Appellee.

It is hereby ordered that the motion made herein by counsel for the appellee by notice of motion dated November 16, 1978 to stay issuance of the mandate pending application to the Supreme Court of the United States for a writ of certiorari pursuant to Rule 41(b) of the Federal Rules of Appellate Procedure be and it hereby is denied.

DENIED.

It is further ordered that

J. EDWARD LUMBARD
WILFRED FEINBERG
WM. H. TIMBERS
Circuit Judges

Judgment of Court of Appeals.

UNITED STATES COURT OF APPEALS

FOR THE

SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the twenty-first day of September one thousand nine hundred and seventy-eight.

Present:

HON. J. EDWARD LUMBARD
HON. WILFRED FEINBERG
HON. WILLIAM H. TIMBERS
Circuit Judges,

77-7468
77-7488

FILOR, BULLARD & SMYTH

Plaintiff-Appellant,

v.

INSURANCE COMPANY OF NORTH AMERICA,

Defendant-Appellee.

Docketed As
A Judgment # 78,1556
On November 29, 1978

Judgment of Court of Appeals.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged, and decreed that the order and judgment of said District Court be and they are hereby reversed and the action be and it hereby is remanded to said district court for further proceedings in accordance with the opinion of this court with costs to be taxed against the appellee.

A. DANIEL FUSARO,
Clerk

By: ARTHUR HELLER,
Deputy Clerk

(A true copy,
(A. DANIEL FUSARO
(Clerk

Statute Involved.

New York Penal Law

§ 170.00 Forgery; definitions of terms

1. "Written instrument" means any instrument or article containing written or printed matter or the equivalent thereof, used for the purpose of reciting, embodying, conveying or recording information, or constituting a symbol or evidence of value, right, privilege or identification, which is capable of being used to the advantage or disadvantage of some person.

2. "Complete written instrument" means one which purports to be a genuine written instrument fully drawn with respect to every essential feature thereof. An endorsement, attestation, acknowledgment or other similar signature or statement is deemed both a complete written instrument in itself and a part of the main instrument in which it is contained or to which it attaches.

3. "Incomplete written instrument" means one which contains some matter by way of content or authentication but which requires additional matter in order to render it a complete written instrument.

4. "Falsely make." A person "falsely makes" a written instrument when he makes or draws a complete written instrument in its entirety, or an incomplete written instrument, which purports to be an authentic creation of its ostensible maker or drawer, but which is not such either because the ostensible maker or drawer is fictitious or because, if real, he did not authorize the making or drawing thereof.

5. "Falsely complete." A person "falsely completes" a written instrument when, by adding, inserting or changing

matter, he transforms an incomplete written instrument into a complete one, without the authority of anyone entitled to grant it, so that such complete instrument appears or purports to be in all respects an authentic creation of or fully authorized by its ostensible maker or drawer.

6. "Falsely alter." A person "falsely alters" a written instrument when, without the authority of anyone entitled to grant it, he changes a written instrument, whether it be in complete or incomplete form, by means of erasure, obliteration, deletion, insertion of new matter, transposition of matter, or in any other manner, so that such instrument in its thus altered form appears or purports to be in all respects an authentic creation of or fully authorized by its ostensible maker or drawer.

7. "Forged instrument" means a written instrument which has been falsely made, completed or altered.
L.1965, c. 1030

Example of Cashier's Check.

MO23686
55-556
212

EATONTOWN
NATIONAL
BANK, EATONTOWN, N. J. 7/30/70 19—

Pay to the
order of Filor, Bullard & Smyth $21,019.40

EATONTOWN
NATIONAL BANK 21019 dols 40 cts DOLLARS

CASHIER'S CHECK s/Douglas J. Schotte Auth. Sig.

Supreme Court, U. S.
FILED
FEB 14 1979
JR., CLERK

IN THE

Supreme Court of the United States

October Term, 1978

No. 78-1242

INSURANCE COMPANY OF NORTH AMERICA,

Petitioner.

against

FILOR, BULLARD & SMYTH,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

LEWIS A. KAPLAN
Attorney for Respondent
345 Park Avenue
New York, New York 10022
(212) 644-8000

RICHARD WASSERMAN
PAUL, WEISS, RIFKIND,
WHARTON & GARRISON
Of Counsel

IN THE

Supreme Court of the United States

October Term, 1978

No. 78-1242

INSURANCE COMPANY OF NORTH AMERICA,
Petitioner,

against

FILOR, BULLARD & SMYTH,
Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

Preliminary Statement

Petitioner, an insurance company, asks this Court to grant certiorari to decide whether a clause in one of its insurance policies is ambiguous under the common law of New York.

This case presents no issue worthy of review, particularly when a heavy load of cases raising constitutional and other important federal issues commands this Court's attention.

This Case Presents No Issue Worthy of Review

1. The ultimate issue below was whether the forgery insuring clause in INA's broker's blanket bond was ambiguous. In resolving that question, the Second Circuit quoted and applied a well-established principle of New York contract law: the words of an insurance policy are ambiguous, and must be construed against the insurer, unless they "not only are susceptible of the construction sought by the defendant [insurer] but that it is the only construction which may fairly be placed upon them" (A8, *quoting Lachs* v. *Fidelity & Casualty Co. of New York,* 306 N.Y. 357, 365, 118 N.E.2d 555, 559 [1954]).

There is no conflict between the decision below and the State courts as to the applicable standard. Accordingly, there is no occasion to review this principle of State law.

2. The Second Circuit's application of the New York ambiguity standard to the facts of this case raises no issue worthy of review. None of the criteria in Sup. Ct. R. 19 suggests that the United States Supreme Court should decide whether INA's proposed interpretation of its policy is the only fair construction. In any event, the Second Circuit's resolution of this issue plainly was correct.

The Supreme Courts of California and Michigan and the Appellate Court of Illinois all recently have held that genuine signatures on corporate documents by corporate officials are "forged" when affixed as part of a scheme to defraud the corporation—precisely the facts of this case. *Century Bank* v. *St. Paul Fire & Marine Insurance Co.,* 4

Cal.3d 319, 482 P.2d 193 (1971); *People* v. *Susalla,* 392 Mich. 387, 220 N.W.2d 405 (1974); *People* v. *Young,* 19 Ill. App.3d 445, 311 N.E.2d 609 (1974). The American Law Institute's Model Penal Code also classifies checks such as these as forgeries (A11-12 & n. 8, A14). The 1967 revision of the New York Penal Law—which adopts the ALI approach—supports the same conclusion (A11-12, A14).

While there are contrary decisions in other jurisdictions, the fact that so many respected authorities hold that checks such as these are "forged" demonstrates conclusively that the interpretation of the insurance policy that INA seeks is not "the only construction which may fairly be placed on" it. *See Pan American World Airways, Inc.* v. *Aetna Casualty & Surety Co.,* 505 F.2d 989, 1001-02 (2d Cir. 1974) (conflicting judicial decisions as to the meaning of "civil war" and similar terms render "war" risk policy exclusion ambiguous under New York law); *cf. Colautti* v. *Franklin,* 99 S.Ct. 675, 686-88 (1979) (statutory standard, the meaning of which was subject to disagreement among experts, impermissably vague).

In dealing with the ambiguity issue, moreover, the Second Circuit properly noted that INA drafted the language at issue (A6) and knew of the conflicting decisions as to the meaning of "forgery," but nevertheless failed to define the term in its policy (A9, A15). Under New York law, these circumstances require particularly strict application of the principle that ambiguous insurance policy language must be construed against the insurer. *E.g., Pan American World Airways, Inc., supra,* 505 F.2d at 1000.

The decision below therefore was correct.

3. INA's contention that the Second Circuit erred in concluding that these checks were "unauthorized" misses the ultimate issue in this case, ignores the applicable New York law, and would present no issue worthy of review in any event.

Given the substantial authority holding that instruments such as these checks are "forged," this insurance policy was ambiguous under the New York standard irrespective of whether one characterizes the signatures as "authorized" or "unauthorized." The authority issue which INA would raise goes not to the question whether the policy language is ambiguous, which is dispositive here, but to the collateral question whether Schotte "forged" these checks within the meaning of the New York Penal Law. N.Y. Penal Law §170.00, subd. 4 (McKinney 1967). The Second Circuit did not purport to decide that question and discussed it only in *dicta* (A10-15). Surely this Court should not grant certiorari to review *dicta* on a question of State law.

Even if the authority issue were central to this case, there would be no issue here worthy of review. In attempting to portray an inconsistency between the decision below and the New York Court of Appeals, INA has ignored the pertinent New York law. As the Second Circuit noted (A4 n. 2), the New York Court of Appeals has held that the genuine signature of the president of a corporation on a corporate check, affixed as part of a scheme to defraud the corporation, is unauthorized. *Wen Kroy Realty Co.* v. *Public National Bank and Trust Co.*, 260 N.Y. 84, 88-91, 183 N.E. 73, 74-75 (1932). Hence, the "authority" issue INA would raise already has been resolved against it by the State's highest court.

4. Finally, INA's effort to create an aura of public importance about this ordinary state law insurance case misses the mark.

The decision below is of no long term significance to the insurance companies, for they can rewrite their policies to exclude risks like this.

Nor is the decision below significant to the banking community. It does not alter or even refer to the law of negotiable instruments. And it is worth noting that the banking community has survived comparable decisions in California, Michigan and Illinois, states with important commercial centers.

Conclusion

The petition for a writ of certiorari should be denied.

Dated: February 14, 1979

Respectfully submitted,

LEWIS A. KAPLAN
Attorney for Respondent
345 Park Avenue
New York, New York 10022
(212) 644-8000

RICHARD WASSERMAN
PAUL, WEISS, RIFKIND,
WHARTON & GARRISON
Of Counsel